

Private Letter Ruling: Partnership with two short taxable years within one calendar year may file a single composite return for partners allowed to participate in composite returns.

March 24, 2003

Dear:

This is in response to your letter dated January 14, 2003, in which you request a Private Letter Ruling (**PLR**) on behalf of COMPANY1, LLC ("COMPANY1" or "Taxpayer"). Review of your request for a **PLR** disclosed that all information described in paragraphs 1 through 8 of subsection (b) of 86 Ill. Adm. Code Section 1200.110 appears to be contained in your request. The **PLR** will bind the Department only with respect to COMPANY1 LLC for the issue or issues presented in this ruling. Issuance of this **PLR** is conditioned upon the understanding that neither COMPANY1, LLC nor a related taxpayer is currently under audit nor involved in litigation concerning the issues that are the subject of this ruling request.

The facts and analysis as you have presented them are as follows:

#### FACTS

1. COMPANY1 is an Illinois Limited Liability Partnership, which is treated as a partnership for federal income tax purposes. It is headquartered in CITY, Illinois, and is in the business of providing employee benefits consulting services businesses throughout the United States. COMPANY1 conducts operations in approximately 19 states and a number of foreign countries.
2. For a number of years many of the partners have satisfied their Illinois income tax filing responsibilities via a composite income tax return filed pursuant to 86 Ill. Admin. Code Sections 100.5100 through 100.5170.
3. Prior to October 1, 2002, COMPANY1 had a fiscal year ending on September 30.
4. COMPANY1 is changing its tax-year end to December 31 (i.e., a calendar year).
5. COMPANY1 will have two tax years ending in 2002 – September 30, 2002 and December 31, 2002. COMPANY1's last fiscal year will be from October 1, 2001 through September 30, 2002. It will have a short period from October 1, 2002 through December 31, 2002 to get it on a calendar year-end.
6. All of the partners included in the composite return are individuals and all are calendar year taxpayers for federal income tax purposes.
7. The partners will report the income from both the September 30, 2002 and the December 31, 2002 tax years on their 2002 federal income tax returns.
8. For the tax year ended September 30, 2002 and December 31, 2002, COMPANY1 will report taxable income.

#### CONCLUSIONS OF THE TAXPAYER

In order to simplify the filing requirements of the COMPANY1 partners, we respectfully request the following rulings:

- 1 That COMPANY1 be granted permission to file a single composite Illinois return combining the two tax periods for all its eligible members who elect to be included.

- 2 That those partners who are included in the composite return and have no other source of Illinois income will not be required to report their share of income from COMPANY1 on a separate return filed with the state.
  - 3 That the composite return will be due on the 15<sup>th</sup> day of the fourth month following the close of the second period (i.e. that it will be due April 15, 2003).
- COMPANY1 makes this request in order to eliminate the unnecessary expense and effort to the state and members of filing individual income tax returns.

### BENEFITS TO THE STATE

This proposal would benefit both the partners of COMPANY1 and the State of Illinois. The benefits to the State of Illinois would be as follows:

1. Reliable Payment of Tax: With COMPANY1 filing a single composite return and paying the state income tax on behalf of the members, the State will receive its income tax in a lump sum directly from COMPANY1. This will guarantee the payment of tax and will save the state the expense of collecting this revenue from numerous individuals.
2. Proper Compliance: By allowing a single composite return, the State is assured of receiving a tax return that covers each partner who receives income from Illinois. This will insure proper compliance with Illinois statutes, rules and regulations and the reporting of all income sourced to Illinois.
3. Ease of Administration: Under a composite return filing, the State will have one return to administer, audit and review. Without a composite return, each partner will be filing his or her own separate return. The State will have more than one thousand returns to administer and audit. Moreover, these individuals reside outside the State of Illinois, which may result in a higher cost of administering and auditing them.

### ANALYSIS

Illinois imposes a tax measured on net income on every individual, corporation, trust, and estate for each taxable year on the privilege of earning or receiving income in Illinois. 35 ILCS 5/201(a). In general, net income is that portion of the taxpayer's base income, less certain exceptions, which is allocable to Illinois, less a standard exemption. 35 ILCS 5/202.

Nonresident individuals report income they receive from sources within the state. A portion of the distributive shares of income received from the partnership would be sourced to Illinois, based on the operations of the partnership. The nonresidents would have to report this income to Illinois.

Illinois regulation 100.5100 gives guidance on the filing of composite returns. In general, composite return may be filed on behalf of nonresident individuals who derive income from Illinois and who are partners of a partnership. The respective partnership shall file such composite return and shall make composite income tax payments.

The regulations do not directly address the issue of how to file a composite return when the partnership has more than one tax year in the same calendar year. However, the

regulations do state that “[t]he filing of a composite return will be considered as a group of separate returns which will meet the individual filing requirements of the Illinois Income Tax Act.” 86 Ill. Admin. Code 100.5120. All of the partners included in COMPANY1’s composite return are individuals who file on a calendar tax year. The income from both the September 30, 2002 and December 31, 2002 tax periods will be reported on their 2002 federal income tax return. The regulations also state that “[t]he amount of composite income apportionable and allocable to Illinois shall be the sum of the income earned or received for the taxable year from the authorized agent by the persons included in the composite return.” (emphasis added) 86 Ill. Admin. Code 100.5130(a)(2). Since the partners’ taxable year includes the income or loss from both the September 30, 2002 and December 31, 2002 tax periods, it is appropriate to file one composite return that includes both periods.

#### OPERATIVE DATE OF THE REQUESTED RULINGS

COMPANY1 and its partners request that this ruling be applicable to the 2002 tax year. To the best of the knowledge of both the Taxpayer and the Taxpayer’s representative, the Department has not previously ruled on the same or similar issues for the taxpayer or a predecessor, and neither the Taxpayer nor the Taxpayer representatives previously submitted the same or similar issue to the Department but withdrew it before a letter ruling was issued.

#### STATEMENT OF AUTHORITIES CONTRARY TO THE TAXPAYER’S VIEWS

According to form IL-1023-C, the Illinois composite return instructions, the Illinois composite return instructions, the Illinois composite return is due the 15<sup>th</sup> day of the fourth month following the close of the authorized agent’s tax year. This would make the due date of the Illinois composite return, for the period ending September 30, on January 15. The second period, ending December 31, would be due on April 15, 2003.

#### TAXPAYER REPRESENTATION

COMPANY2 LLP represents COMPANY1 and its partners in making this ruling request. A power of attorney representing Mr. Z and Ms. Y of that Firm for purposes of this ruling has been attached.

In response to your inquiry, please be advised that the composite return regulations, authorized under IITA 502(f), were designed exactly for the exactly the reasons stated in your correspondence: taxpayer convenience and ease of administration for the Department. There is nothing in either the statute or the regulations which precludes the type of filing for which you have requested permission; in fact, it is not specifically addressed at all. The Instructions to Illinois’ composite return form, IL-1023-C, which refer to a due date of the 15<sup>th</sup> day of the fourth month following the close of the designated agent’s tax year were obviously written in contemplation of a “regular” 12-month tax year, be it fiscal or calendar. They also fail to account for a situation like that experienced by your client, which is taking the “less-regular” step of converting from one type of tax year to another. In other words, we believe the spirit of the composite return regulations is liberal enough, absent specific contrary authority, to allow the relief you have requested. Furthermore, the Department has ruled similarly on prior occasions. (See, e.g., IT 01-0034, IT 87-0003, IT 87-0025, IT 87-0276, and IT 88-

0213, wherein the taxpayer-corporation was required by federal consolidated return regulations to divide its otherwise-unchanged taxable year into two short taxable years because it was acquired by another corporation, and the taxpayer was not being added to the unitary business group of the acquiring corporation). Finally, in light of your request, Legal is considering amending the composite return regulations and revising the pertinent form instructions to address (and allow) filing based upon a converted tax year which includes two short taxable years.

#### DEPARTMENT RULING

The relief requested in your correspondence is granted. Therefore:

1. COMPANY1 is hereby granted permission to file a single composite return combining the two tax periods for all its eligible members who elect to be included.
2. Those partners who are included in the composite return and have no other source of Illinois income will not be required to report their share of income from COMPANY1 on a separate return filed with the state.
3. Given the fact that COMPANY1 is converting from a fiscal tax year to a calendar year, the composite return will be due on the 15<sup>th</sup> day of the fourth month following the close of the second period (i.e. that it will be due April 15, 2003).

The facts upon which this **PLR** are based are subject to review by the Department during the course of any audit, investigation or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

Sincerely yours,

Jackson E. Donley,  
Senior Counsel-Income Tax